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(I)

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In the Supreme Court of the United States

OCTOBER TERM, 1940

No. 110

LEE H. MARSHALL HEIRS ET AL., FIDELITY TRUST
COMPANY, TRUSTEE, PETITIONER

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL
REVENUE

*ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED
STATES CIRCUIT COURT OF APPEALS FOR THE THIRD
CIRCUIT*

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The majority and dissenting opinions in the Board of Tax Appeals (R. 15-32) are reported at 39 B. T. A. 101. The majority and dissenting opinions in the Circuit Court of Appeals (R. 145-152) are not yet reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on April 26, 1940. (R. 152.) The

petition for a writ of certiorari was filed May 28, 1940. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the trust of which the petitioner is the trustee was an association taxable as a corporation under Section 801 (a) (2) of the Revenue Act of 1934.

STATUTE AND REGULATIONS INVOLVED

The statute and regulations involved are set out in the Appendix, *infra*, pp. 12-16.

STATEMENT

The facts found by the Board of Tax Appeals (R. 16-25), from a stipulation (R. 40-47), testimony (R. 47-65), and exhibits (R. 67-141), may be summarized as follows:

The petitioner (formerly Fidelity Title & Trust Company) during the taxable year was trustee under an instrument (R. 81-89) made November 30, 1925, whereby the four children of George V. and Emma L. Marshall, and their respective spouses, conveyed to the petitioner a certain tract of land known as the "Marshall land" in trust for themselves, the trust to continue during the life of the longest living of the eight beneficiaries, but in no event beyond April 30, 1968. (R. 16-17.)

The Marshall land, which was the only asset of the trust, was part of a larger tract on which was

constructed the Frank & Seder Department Store building, in the City of Pittsburgh. The building stood on several tracts of land, all under leases running to April 30, 1968, under all of which the lessee was to pay, in addition to rental, the taxes and water rent, gas, electricity, insurance, and was to make all repairs and remove debris. (R. 19.)

The instrument by which the Marshall land was conveyed in trust to the petitioner gave the trustee the power to hold, manage and control the property; to lease it in whole or in part with the consent of the majority of the beneficiaries, or, if a majority of the beneficiaries could not agree, then according to its own judgment for a term not exceeding three years; to collect, receive, sue for and recover the rents, issues, and profits therefrom; to oversee the payment of taxes, municipal assessments, insurance and interest on mortgages; to make payments on the principal of any mortgage, as agreed to by a majority of the beneficiaries; to contract for the repair and general upkeep of the property; to pay all charges and expenses in connection with the property, and thereafter to pay the net income from the property to the beneficiaries, their heirs, executors, and assigns, as their interest may appear; to sell at public or private sale the whole or any part of the property, and give deeds therefor, with the consent of a majority of the beneficiaries; and to borrow money and execute bonds and mortgages therefor for the payment of any lien or for other purposes, including the construction of a building

on the premises or for alterations or improvements thereto, with the approval of a majority of the beneficiaries. The trustee was not to be liable beyond the property in its hands for judgment, taxes, or any other charges. The trust was subject to revocation at any time¹ by a majority in interest of the beneficiaries, their heirs and assigns. (R. 16-19.)

The four Marshall children had received the Marshall land on November 30, 1925, by a conveyance to them as tenants in common, from the Marshall Land Company, a corporation, of which they had been the sole stockholders since February 28, 1922, when their mother, Emma L. Marshall, had transferred to them all of the stock of that corporation. The mother had formed that corporation in September, 1920, and conveyed to it the interest in the Marshall land which she had acquired upon the death of her husband, George V. Marshall, on May 6, 1918, and the corporation subsequently acquired other outstanding interests in the land. (R. 21-23.)

A lease of his interest in the Marshall land to Frank & Seder, under which a new building was to be erected by the lessee, had been made by George V. Marshall on May 22, 1917, for a period ending April 30, 1938. On April 24, 1924, the Marshall Land Company made a lease to National Depart-

¹ The trust was revoked and terminated on August 7, 1936, after the Government had claimed that it was taxable as a corporation. (R. 51.)

ment Stores, Inc. (successor to Frank & Seder), for an additional thirty years running to April 30, 1968, for a fixed net rental, all taxes, insurance, and repairs to be paid by the lessee. After this new lease was made, the four Marshall children, who were then the stockholders of the Marshall Land Company, determined to dissolve the corporation and convey the property to a trustee, which they did, after the conveyance of the property from the corporation to them, on November 30, 1925. (R. 20-21, 22-23.)

When the Marshall land was conveyed to the petitioner as trustee, it was subject, in addition to the lease, to a mortgage which became due in 1927, at which time the balance then due was paid off from the proceeds of a new mortgage made in 1927, under which payments for interest and amortization of principal were to be made for fourteen years, and the balance to be paid at the end of the fifteenth year. (R. 23.)

For the purpose of either renting or selling, the Marshall land was more valuable as a unit than if the heirs had endeavored to rent or sell their separate shares. None of the trust beneficiaries was qualified to manage the property for rental purposes; they had no such business experience. The beneficiaries held meetings or conferences from time to time for the purpose of discussing matters relative to the trust. (R. 24.)

The tenant of the Marshall land defaulted in the payment of rent in 1932, and the petitioner, instead

of exercising its option to eject the tenant, entered into negotiations which continued for about three and a half years and which culminated in a new agreement made in November, 1935, under which the leasing was to be continued, under modified rentals, to a new corporation to be formed in a reorganization proceeding of the tenant. (R. 24-25.)

On March 15, 1935, the petitioner filed a fiduciary return of income for the year 1934, showing a net income of \$9,698.86 and the distribution thereof equally to the four beneficiaries, who reported their distributive share in their individual income tax returns for 1934 and paid the tax due thereon. (R. 24.)

The Commissioner of Internal Revenue, holding that the petitioner was an association taxable as a corporation, determined a deficiency in income and excess profits tax against the petitioner on that basis for the year 1934,² in the respective amounts of \$1,333.59 and \$484.94. (R. 9-13.)

The Commissioner's determination was sustained by the Board of Tax Appeals (R. 25-30), and the decision of the Board was affirmed by the court below (R. 145-150).

² The determination of similar deficiencies for the years 1932 and 1933 was upset by the court below, on the authority of the decision of this Court in *Germantown Trust Co. v. Commissioner*, decided February 26, 1940, on the ground that they were barred by limitations.

ARGUMENT

There are no conflicts and the decision below is in accord with established principles.

The court below, affirming the Board and the Commissioner, correctly concluded that the trust here involved was an association taxable as a corporation under the statute (Section 801 (a) (2) of the Revenue Act of 1934, *infra*) and the Regulations (Articles 801-1, 801-2, and 801-3 of Treasury Regulations 86, *infra*).³ *Morrissey v. Commissioner*, 296 U. S. 344; *Helvering v. Coleman-Gilbert*, 296 U. S. 369; *Swanson v. Commissioner*, 296 U. S. 362; *Helvering v. Combs*, 296 U. S. 365. The four Marshall children, who were the owners of the property as tenants in common, associated themselves in a joint enterprise for the transaction of business and division of gains, exactly as had been done theretofore by the corporation, the Marshall Land Company, of which they were the sole shareholders. (R. 21-22, 44, 48, 50, 65.) By the transfer to the trust they secured continuing and uninterrupted centralized management—subject to revocation—until the death of the longest living beneficiary, but not beyond April 30, 1968. The con-

³ As the court below observed (R. 150), these Regulations, though considerably expanded, are not dissimilar to those promulgated under the Revenue Act of 1924 (Articles 1502 and 1504 of Treasury Regulations 65, as amended), which Congress, in subsequently using the term "association" in the 1924 Act, must be presumed to have viewed with approval. *Morrissey v. Commissioner*, 296 U. S. 344, 355.

tinuity was not to be interrupted by the death of any of the beneficial owners nor by the transfer of any beneficial interest. The trustee was vested with broad powers, essential to the carrying on of business for profit. (R. 28, 149.) The main purpose of the trust, as shown by the instrument, was neither liquidation nor holding and preserving the property (R. 27), but the carrying on of a business for profit and the sharing of gains. Clearly, under the facts, this is a case where those beneficially interested "seek to share the advantages of a union of their interests in the common enterprise." *Morrissey v. Commissioner, supra*, p. 357.

The fact that the tenant paid the taxes, insurance, and cost of repairs, allegedly leaving to the trustee little to do during the taxable year except to collect the rent and distribute it, is not, as asserted (Br. 17-19), decisive. As properly pointed out both by the Board and the court below (R. 28, 148), the powers conferred on the trustee in the instrument, rather than the activities engaged in during the particular year, are controlling—otherwise, the same organization might be classed as a trust in one year and as an association in another year. *Morrissey v. Commissioner, supra*, p. 361; *Sloan v. Commissioner*, 63 F. (2d) 666, 669 (C. C. A. 9th); *Commissioner v. Vandergrift R. & Inv. Co.*, 82 F. (2d) 387, 390 (C. C. A. 9th). Moreover, it may be pointed out that the trustee's "handling a large property * * * and seeing that the

lessees lived up to their contracts" was "doing business." *Von Baumbach v. Sargent Land Co.*, 242 U. S. 503, 517.

Neither the limited number of beneficiaries nor the fact that the operations did not extend beyond the one piece of property compels, as suggested (Br. 15, 16), a different conclusion. *Swanson v. Commissioner*, *supra*, p. 365; *Helvering v. Coleman-Gilbert*, *supra*, pp. 372, 373; *Helvering v. Combs*, *supra*, p. 368. That the trust was of a limited duration is not, as implied (Br. 15-16), material. A corporation, too, could be made of limited duration. Nor is the absence of particular formalities of procedure or records significant, as argued (Br. 16-17). *Helvering v. Coleman-Gilbert*, *supra*, p. 373. and *Helvering v. Combs*, *supra*, p. 369.

The decision of the court below is a correct application of the principles enunciated by this Court to the facts of the instant case, and is in accord rather than in conflict with the *Morrissey* case. Nor is it in conflict with *Lewis & Co. v. Commissioner*, 301 U. S. 385. The different result in the *Lewis* case is accounted for by the facts there involved, which distinguish it from the instant case. There were no "associates" in that case, for the two beneficiaries consisted of the single grantor and owner of the property and one who was a mere agent of the grantor and whose rights were limited to commissions on sales. Moreover, the powers and duties of the trustee there were purely ministerial.

Nor is there any conflict, as urged (Pet. 6), with *Lansdowne Realty Trust v. Commissioner*, 50 F. (2d) 56 (C. C. A. 1st), or *Myers v. Commissioner*, 89 F. (2d) 86 (C. C. A. 7th). The purpose of the trust in the *Lansdowne* case was primarily to liquidate, the trustees being obliged to convert the property into cash and distribute it, with the right to defer the conversion for a period not to exceed twenty years. The statement made by the court there to the effect that although the trustees had broad powers they did not exercise them and hence the trust was not an association carrying on business, must be viewed in the light of the fact that the case was decided in 1931, at least several years before this Court had held in the *Morrissey* case that the purposes and powers of a trust, whether exercised or not, are determinative. *Tyson v. Commissioner*, 54 F. (2d) 29 (C. C. A. 7th), with which conflict is also claimed (Br. 21) is similarly distinguishable. The *Myers* case is likewise distinguishable on the facts because it involved a trust formed by three brothers in order "to make more certain their ability to hold the property together until the liquidation of the mortgage". (89 F. (2d), p. 87.) That case turned upon its own peculiar facts, which the court recognized distinguished it from the *Morrissey* and companion cases decided by this Court (89 F. (2d), pp. 89-90), and which, we submit, distinguish it from the instant case.

CONCLUSION

The decision of the court below correctly applies the statute and the governing principles established by decisions of this Court, to the facts of the case. There is no conflict of decisions. The petition should, therefore, be denied.

Respectfully submitted.

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JUNE, 1940.